

Message Text

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ACTION NEA-10

INFO OCT-01 EA-10 ISO-00 SP-02 USIA-06 AID-05 EB-08
NSC-05 TRSE-00 SS-15 STR-05 OMB-01 CEA-01 CIAE-00
COME-00 FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03
LAB-04 SIL-01 L-03 H-01 PRS-01 PA-01 AGRE-00
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FM AMEMBASSY COLOMBO

TO SECSTATE WASHDC 9105

INFO AMEMBASSY BONN

AMEMBASSY KUWAIT

AMEMBASSY MANILA

AMEMBASSY NEW DELHI

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MANILA FOR USADB

E.O. 11652: N/A

TAGS: EAID, EFIN, EAGR, CE

SUBJ: FINANCE MINISTER CALLS FOR TERMINATION OF UREA PROJECT

1. BEGIN LIMITED OFFICIAL USE. SUMMARY: IN A SURPRISE STATEMENT, THE FINANCE MINISTER HAS CALLED FOR CANCELLATION OF SRI LANKA'S FIRST UREA FACTORY NOW UNDER CONSTRUCTION ON THE GROUNDS THAT IT WOULD COST THE COUNTRY \$25 MILLION IN 1978, AND LOSSES WOULD GROW TO \$37.5 MILLION BY 1990. HE SAID THE PREVIOUS GOVERNMENT STARTED THE PROJECT EVEN THOUGH THE WORLD BANK AND AID CONSORTIUM COUNTRIES REFUSED TO PROVIDE FINANCING. IN FACT, HOWEVER, THE FOREIGN EXCHANGE COSTS OF THIS PROJECT ARE BEING JOINTLY FINANCED BY THE ASIAN DEVELOPMENT BANK (ADB), THE WEST GERMAN AND INDIAN GOVERNMENTS, AND THE KUWAIT FUND FOR ARAB ECONOMIC DEVELOPMENT. THE UREA
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FACTORY IS THE LARGEST SINGLE FOREIGN AID EFFORT IN SRI LANKA AFTER THE MAHAWELI PROGRAM. THE EMBASSY WILL REPORT FURTHER.
END SUMMARY. END LIMITED OFFICIAL USE.

2. BEGIN UNCLASSIFIED. IN THE COURSE OF PARLIAMENTARY CONSIDERATION OF THE BUDGET APPROPRIATION FOR THE MINISTRY OF INDUSTRIES AND SCIENTIFIC AFFAIRS, FINANCE MINISTER RONNIE

DE MEL ASKED THE MINISTER OF INDUSTRIES TO TAKE IMMEDIATE ACTION TO CANCEL THE CONTRACT FOR THE RS. 2 BILLION (\$125 MILLION AT CURRENT EXCHANGE RATE) UREA FERTILIZER FACTORY.

3. ACCORDING TO THE FINANCE MINISTER, THE PLANNED CAPACITY OF 310,000 METRIC TONS OF UREA IS FAR IN EXCESS OF THE COUNTRY'S CURRENT ANNUAL CONSUMPTION OF 100,000 MT AND OF THE PROJECTED REQUIREMENT OF 150,000 MT IN 1985. AS A RESULT OF THIS OVER CAPACITY, AND BECAUSE THE WORLD PRICE OF UREA HAS DECLINED FROM \$330 TO \$110 PER TON, THE MINISTER SAID THE PROPOSED FACTORY WOULD LOSE RS. 400 MILLION (\$25 MILLION) NEXT YEAR AND LOSSES WOULD GROW IN EACH SUCCEEDING YEAR TO REACH RS. 600 MILLION (\$37.5 MILLION) BY 1990. HE FURTHER STATED THAT IT WOULD BE MUCH CHEAPER TO IMPORT UREA AND EXPORT THE LOCALLY REFINED NAPHTHA WHICH WAS TO HAVE BEEN THE FACTORY'S FEEDSTOCK. THE MINISTER CALLED FOR CANCELLATION OF THE CONTRACT EVEN IF THE GOVERNMENT HAS TO PAY A PENALTY OF RS. 100 MILLION (\$6.2 MILLION).

4. IN REVIEWING THE HISTORY OF THE UREA PROJECT, THE MINISTER SAID A FERTILIZER FACTORY WAS FIRST CONSIDERED SHORTLY AFTER INDEPENDENCE IN 1948 WHEN THE COST WOULD HAVE BEEN RS. 90 MILLION (\$19 MILLION AT THE EXCHANGE RATE PREVAILING AT THAT TIME), BUT DUE TO "A TUG-OF-WAR BETWEEN SEVERAL MINISTERS" THE PROJECT WAS SHELVED. THE PROJECT WAS RENEWED AGAIN DURING THE DUDLEY LIMITED OFFICIAL USE

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SENANAYAKE GOVERNMENT OF 1965-70 AT AN ESTIMATED COST OF RS. 346 MILLION (\$58 MILLION) BUT WAS NOT IMPLEMENTED BEFORE THE UNITED FRON (UF) GOVERNMENT CAME INTO POWER IN 1970. THE UF GOVERNMENT FIRST DECIDED TO DROP THE PROJECT AS TOO COSTLY, THEN REVIVED IT IN 1975, AFTER COSTS HAD RISEN TO RS. 1,168 MILLION (\$152 MILLION). THE MINISTER STATED THAT SUBSEQUENT INFLATION HAS PUSHED THE TOTAL COST TO RS. 2 BILLION (\$125 MILLION). (EMBASSY COMMENT: THE MINISTER'S COST ESTIMATES WERE GIVEN IN RUPEES; NO EXPLANATION WAS PROVIDED FOR THE APPARENT DECLINE IN DOLLAR TERMS FROM THE 1975 COST PROJECTION TO THE MINISTER'S LATEST ESTIMATE.)

5. THE MINISTER SAID THE UF GOVERNMENT WENT AHEAD AFTER "ALL AID CONSORTIUM COUNTRIES REFUSED TO FINANCE THE PROJECT BECAUSE IT WAS UNWORKABLE AND WOULD RESULT IN GRAVE LOSS." THE MINISTER ASKED FOR AN INVESTIGATION OF COMMISSION PAYMENTS UNDER THE UREA CONTRACT TOTALING RS. 50 MILLION (\$3 MILLION) AND WARNED CHAIRMEN, DIRECTORS, AND GENERAL MANAGERS OF STATE CORPORATIONS AND BOARDS THAT LEGISLATION WOULD BE INTRODUCED HOLDING

THEM PERSONALLY RESPONSIBLE FOR ENTERING INTO SIMILAR CONTRACTS.

6. THE CONTRACT TO BUILD THE FERTILIZER COMPLEX WAS AWARDED TO KELLOG INTERNATIONAL AND CONSTRUCTION HAS ALREADY BEGUN. ACCORDING TO THE AFTERNOON CEYLON OBSERVER OF DECEMBER 22, INDUSTRIES MINISTER CYRIL MATHEW, IN CONSULTATION WITH THE PRIME MINISTER, WILL APPOINT A SPECIAL COMMITTEE TO EXAMINE THE FUTURE OF THE UREA PROJECT. END UNCLASSIFIED.

7. BEGIN LIMITED OFFICIAL USE. EMBASSY COMMENT. THERE ARE SOME RATHER INTERESTING ERRORS AND OMISSIONS IN THE FINANCE MINISTER'S STATEMENT. DESPITE WHAT HE LIMITED OFFICIAL USE

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SAID ABOUT THE LACK OF AID/CONSORTIUM ASSISTANCE, THE \$92.0 MILLION IN FOREIGN EXCHANGE COSTS ARE BEING FINANCED BY THE ASIAN DEVELOPMENT BANK (\$30 MILLION), THE KUWAIT FUND FOR ARAB ECONOMIC DEVELOPMENT (\$25 MILLION), THE WEST GERMAN GOVERNMENT (\$24.5 MILLION), AND THE INDIAN GOVERNMENT (\$12.5 MILLION). MOREOVER, HE FAILED TO MENTION THAT THE PROJECT APPRAISAL, WHICH WAS PREPARED BY THE JAPAN CONSULTING INSTITUTE ON BEHALF OF THE ADB (REPORT NUMBER SRI:AP-10, AUGUST 1975), PROJECTED UREA CONSUMPTION WOULD GROW TO 268,500 TONS BY 1985.

8. AN OFFICIAL OF THE GERMAN EMBASSY EXPRESSED SURPRISE AT THE MINISTER'S STATEMENT AND TOLD EMBASSY HE HAD NO IDEA WHAT THE FUTURE OF THE UREA PROJECT WOULD BE. AFTER THE MAHAWELI PROGRAM, THE UREA FACTORY IS THE LARGEST SINGLE PROJECT FINANCED BY FOREIGN AID IN SRI LANKA. THE EMBASSY WILL REPORT FURTHER AS MORE INFORMATION BECOMES AVAILABLE.
WRIGGINS

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